



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
1100 Commerce Street
Dallas, TX 75242

501.03-00

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: January 28, 2011

Number: 201116046
Release Date: 4/22/2011

LEGEND

ORG = Organization name XX = Date Address = address

Person to Contact:
Badge Number:
Contact Telephone Number:
Contact Address:
Employer Identification Number:

CERTIFIED MAIL

Dear :

This is a final notice of adverse determination that your exempt status under section 501(c)(3) of the Internal Revenue Code is revoked. Recognition of your exemption under Internal Revenue Code section 501(c)(3) is revoked effective July 1, 20XX the following reason(s):

You are not operated exclusively for an exempt purpose as required by Internal Revenue Code section 501(c)(3). You are not and have not been engaged primarily in activities which accomplish one or more exempt purposes. You are not a charitable organization within the meaning of Treasury Regulation 1.501(c)(3)-1(d); rather, your activities further a substantial nonexempt commercial purpose and serve private rather than public interests.

Contributions to your organization are no longer deductible effective July 1, 20XX.

Since your exempt status has been revoked, you are required to file Form 1120, U.S. Corporation Income Tax Return, for all years beginning on or after July 1, 20XX.

Income tax returns for subsequent years are to be filed with the appropriate Service Center identified in the instructions for those returns.

It is further determined that your failure to file a written appeal constitutes a failure to exhaust your available administrative remedies. However, if you decide to contest this determination in court, you must initiate a suit for declaratory judgment in the United States Tax Court, the United States Claims Court, or the district court of the United States for the District of Columbia before the (ninety-first) 91st day after the date that this determination was mailed to you. Contact the clerk of the appropriate court for rules for initiating suits for declaratory judgment.

To secure a petition form, write to the following address: United States Tax Court, 400 Second Street, NW, Washington, DC 20217.

Please understand that filing a petition for a declaratory judgment under IRC section 7428 will not delay the processing of subsequent income tax returns and assessment of any taxes due.

You also have the right to contact the Office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers. You can call 1-877-777-4778, and ask for the Taxpayer Advocate assistance or you can contact the Advocate from the site where this issue was determined by writing to:

Taxpayer Advocate assistance cannot be used as substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determination, nor extend the time fixed by law that you have to file a petition in Court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling.

This letter should be kept within your permanent records.

If you have any questions, please contact the person whose name and telephone number are shown above.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Enclosures:
Publication 892



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
Internal Revenue Service
TEGE EO Examinations
12301 Research Blvd., Bldg. IV, MS: 4949 AUNW
Austin, TX 78759

October 26, 2010

ORG
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail - Return Receipt Requested

Dear :

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended 20XX06 and 20XX06

LEGEND

ORG = Organization name XX = Date State = state CO-1 = 1st COMPANY

ISSUES:

1. Whether revocation of the organization's tax-exempt status, under IRC section 501(c)(3), is necessary because of inactivity.
2. Whether revocation of the organization's tax-exempt status is necessary because of substantial inurement.

FACTS:

The ORG is recognized as a section 501(c)(3) tax-exempt organization. According to its articles of incorporation, the organization was organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual. The organization registered with the State of State as a Non-profit Corporation on November 21, 19XX.

According to the organizations response (in a fax dated 8/25/20XX) to the services IDR (dated August 10, 20XX), the "only activity [for the tax year ending June 30, 20XX] was donations to CO-1" (See Attachment 1).

The organizations response stated that "The ORG held monthly bingo games for several years but discontinued them sometime prior to 20XX... The last fundraiser was held in 20XX. The ORG has had less than \$\$ of gross receipts yearly for many years (having no income FYE 6/30/XX, 6/30/XX, 6/30/XX, and 6/30/XX)" (See Attachment 2). During the tax years ending June 30, 20XX and June 30, 20XX, the ORG's only income was from interest income and the organizations money was only distributed to the CO-1.

According to the organizations response (in a fax dated 8/25/20XX) to the services IDR (dated August 10, 20XX), "the ORG was formed by members of the CO-1 to raise funds to support the fraternal and charitable purposes of the CO-1... The Council does not allow its clubs to hold fundraisers that include any gaming activity, so the ORG was used to hold these types of fundraisers in order to support the CO-1... The ORG has been donating its funds to the CO-1 as they need them to continue in existence and has very little money left in its bank account... The ORG is allowed to donate funds from its gaming checking account to the CO-1 under the gaming laws of LADORT, so most of its funds have been used as donations to do the needed repairs to the CO-1 building." (See Attachment 2)

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LAW:

Section 501(c)(3) of the Internal Revenue Code exempts from Federal income tax: corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting to influence legislation and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

Section 6001 provides that every person liable for any tax imposed by the Code, or for the collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time prescribe.

Treasury Regulations section 1.501(c)(3)-1(a)(1) provides that in order to be exempt as an organization described in section 501(c)(3) of the Code, the organization must be one that is both organized and operated exclusively for one or more of the purposes specified in that section.

Treasury Regulation section 1.501(c)(3)-1(c)(1) provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than insubstantial part of its activities is not in furtherance of an exempt purpose.

Treasury Regulation section 1.501(c)(3)-1(c)(2) provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. The words "private shareholder or individual" refer to persons having a personal and private interest in the activities of the organization.

Treasury Regulation section 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. Thus, to meet the requirement of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Revenue Ruling 61-170, 1961-2 CB 112 ruled that in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

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Name of Taxpayer ORG		Year/Period Ended 20XX06 and 20XX06

Revenue Ruling 70-4, 1970-1 CB 126 ruled that Section 501(c)(3) of the Code provides for the exemption from Federal income tax of organizations organized and operated exclusively for educational purposes. Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Revenue Ruling 70-533, 1970-2 CB 112 ruled that Section 1.501(c)(3)-1(d)(1)(ii) of the Income Tax Regulations provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest

American Campaign Academy v. Commissioner, 92 T.C. 1053, 1065-66 (1989) (when an organization operates for the benefit of private interests, such as designated individuals, the creator or his family, or persons directly or indirectly controlled by such private interests, the organization by definition does not operate exclusively for exempt purposes); Old Dominion Box Co., Inc. v. United States, 477 F.2d 340 (4th Cir. 1973) (operating for the benefit of private parties who are not members of a charitable class constitutes a substantial nonexempt purpose.) In Leon A. Beeghly Fund v. Commissioner, 35 T.C. 490, 518 (1960), aff'd, 310 F.2d 756 (6th Cir. 1962), the Tax Court held:

[w]e think that although the ultimate purpose of the trust to benefit charities may have remained unchanged by this transaction, nevertheless, the primary objective of the trust entering into this transaction was for the benefit of stockholders of [the business company] with the objective of ultimately benefiting charities running a poor second, and that when the trust was utilized for such a purpose it fell without the scope of both the language of section 101(6) [now Code §501(c)(3)] and the congressional intent in enacting this exemption provision.

Revenue Ruling 68-489, 1968-2 CB 210 states that an organization will not jeopardize its exemption under section 501(c)(3) of the Code, even though it distributes funds to nonexempt organizations, provided it retains control and discretion over use of the funds for section 501(c)(3) purposes.

In New Faith, Inc. v. Commissioner, T.C. Memo 1992-601, the court stated that an organization must substantiate its alleged charitable activities with specific documentation in the form of checks, invoices, receipts, contemporaneous journals, and other documentation.

TAXPAYER'S POSITION

The service has not yet received a position from the ORG, regarding its position on the proposed revocation. This will be updated once there is a response to this issue.

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GOVERNMENT'S POSITION

The Operational Test, Treas. Reg. Section 1.501(c)(3)-1(c), is specifically related to an organization's activities. Even if an organization passes the *organizational test* by having adequate language regarding their charitable activities. The operational test indicates that the ORG's activities are not strictly charitable.

To satisfy the operational test, an organization must:

- Engage primarily in activities which accomplish one or more of the exempt purposes specified in IRC section 501(c)(3) (*Treas. Reg. section 1.501(c)(3)-1(c)(1)*)
- Not allow its net earnings to inure to the benefit of private shareholders or individuals (*Treas. Reg. section 1.501(c)(3)-1(c)(2)*)
- Not engage in **substantial** lobbying activity (*Treas. Reg. section 1.501(c)(3)-1(c)(3)*) **and**
- Not engage in **any** political activity (*Treas. Reg. section 1.501(c)(3)-1(c)(3)*)

Harding Hospital, Inc. v. U.S., 505 F. 2d 1068, 1072 (6th Cir. 1974) shows that if an organization fails to comply with any of these requirements, it will fail the operational test and lose its IRC section 501(c)(3) exemption.

The ORG has not engaged in any activities which accomplish one or more of the exempt purposes specified in IRC section 501(c)(3), in the years under examination. During the tax years ending June 30, 20XX and June 30, 20XX, the ORG's only income was from interest and the organizations money was only distributed to the CO-1. Distributing money to an organization exempt under IRC section 501(c)(10) is not a charitable purpose unless it is designated to be used specifically for 501(c)(3) purposes. The ORG did not designate the money to be used for 501(c)(3) purposes.

The facts show that the ORG is not operated exclusively for a tax exempt charitable purpose. The ORG has not engaged in activities that accomplish purposes described in section 501(c)(3). The ORG was operated for the benefit of paying for the CO-1's (exempt under IRC section 501(c)(10) building expenses rather than exclusively for tax exempt purposes. In addition, the ORG made a donation to an organization which is not described in section 501(c)(3) and no evidence shows that the ORG maintained sufficient control over the funds to ensure that the donation would serve purposes described in section 501(c)(3). Revocation of exempt status is in order.

The organization must not be organized or operated for the benefit of private interests, such as the creator or the creator's family, shareholders of the organization, other designated individuals, or persons controlled directly or indirectly by such private interests. As stated in Code section 501(c) (3) above, no part of the net earnings of an IRC Section 501(c) (3) organization may inure

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to the benefit of any private shareholder or individual. A private shareholder or individual is a person having a personal and private interest in the activities of the organization. A substantial part of the ORG assets have inured to the CO-1. American Campaign Academy v. Commissioner shows that an organization that operates for the benefit of private interests, such as designated individuals, the creator or his family, or persons directly or indirectly controlled by such private interests; the organization by definition does not operate exclusively for exempt purposes.

CONCLUSION

The service is proposing revocation of the of the determination of the exempt status, under IRC 501(c)(3), of the ORG, Inc, with a revocation date effective July 1, 20XX.

If you agree to the proposed revocation, please sign form 6018, and mail back to the person listed in the attached letter, with in 30 days of receipt of this letter. If you do not agree to the proposed revocation please refer to the letter and attached publications for the appeals process, or contact the person listed in the letter.

We will not be pursuing delinquent Form 1120 returns for the tax periods ending June 30, 20XX and June 30, 20XX, because the amount of income for these years was de minimis.